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IN THE

Supreme Court of the United States

OCTOBER TERM, A. D. 1947.

No. 395

STIMSON MILL COMPANY,
Petitioner.

vs.

COMMISSIONER OF INTERNAL REVENUE,
Respondent.

PETITION FOR WRIT OF CERTIORARI
To the United States Circuit Court of Appeals
For the Ninth Circuit
And Brief In Support Thereof.

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Of Counsel.

Scheffer Printing Company, Del. 7171

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MISCELLANEOUS CITATIONS IN BRIEF

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To the Honorable Fred M. Vinson, Chief Justice of the United States, and the Associate Justices of the Supreme Court of the United States:

The Petition of Stimson Mill Company (hereinafter called "Stimson") respectfully shows:

I. Summary statement of the matter involved.

In filing its excess profits tax return for the year 1942, Stimson computed its excess profits credit under section 713, such credit being 95% of "average base period net income" for the years 1936 to 1939, inclusive. Profits in excess of such credit were subjected to the excess profits tax at the rate of 90%. Profits covered by the amount of

the credit, however, were subject only to income tax and surtax at rates aggregating 40%.[1]

Stimson claimed that its "average base period net income" was an "inadequate standard of normal earnings" (section 722(b)) because its earnings for the year 1937 were abnormally low on account of a strike which occurred in that year, that its excess profits credit based thereon was also too low, and that as a result the excess profits tax was excessive and discriminatory, since too great a portion of the profits were subjected to the 90% excess profits tax, and too small a portion of the profits (represented by the said inadequate credit) were subject only to the 40% tax.

Stimson, therefore, filed an application for relief under section 722,[2] which provides for a determination of normal earnings for one or more years of the base period and for the use of such normal earnings in a "constructive average base period net income", which is used in lieu of "average base period net income" for computing the excess profits credit in section 713 by taking 95% of such "constructive average". The Commissioner denied the application on December 26, 1944 (R. 7), but after Stimson appealed to the Tax Court, he stipulated (R. 16, 17) that Stimson's

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[1] Normal tax at 24% was imposed by Sec. 103, Revenue Act of 1941, 26 U.S.C.A. Internal Rev. Acts beginning 1940, p. 102. Surtax at 16% was imposed by Sec. 105(b), Revenue Act of 1942, 26 U.S.C.A. Internal Rev. Acts beginning 1940, p. 172. Such rates of 24% and 16% aggregating 40% were here applied (Rec. 11).

Excess profits tax at 90% was imposed by Sec. 202, Revenue Act of 1942, 26 U.S.C.A. Internal Revenue Acts beginning 1940, p. 280. Such tax at 90% was here applied (Rec. 12).

Pertinent provisions of section 713 are set forth in the appendix. Other statutory adjustments in determining tax liability are not material to the question presented.

[2] Pertinent provisions of section 722 are set forth in the appendix.

"normal operation or output was interrupted in the year 1937 by strikes", that because thereof "earnings for 1937 in the amount of $63,706.57 were abnormally low" and that reconstructed earnings for that year amounted to $85,263.34.

Nevertheless, the Commissioner denied relief by his method of computing the excess profits credit. He provided a computation for a "*constructive* average base period net income" which differed from the computation provided by the definition of "average base period net income" in section 713(e).

Before giving effect to relief provisions, Stimson's "average base period net income" computed under section 713(e) (R. 16), compared with an ordinary average as follows:

Year	Ordinary Arithmetic Average	Standard of Normal Earnings Section 713(e)
1936	$ 89,422.67	$ 89,422.67
1937	63,706.57	63,706.57
1938	38,127.75	.....
1939	111,839.77	111,839.77
Aggregate	$303,096.76	$264,969.01
Average	$ 75,774.19	$ 88,323.00
Substitute 75% of 3-year average for 1938		$ 66,242.25
Aggregate for 1936, 1937 and 1939 as above		264,969.01
Aggregate for four years		$331,211.26
Average		$ 82,802.82
Excess profits credit (95% of average)		$ 78,662.68

As shown above, the computation of average base period net income under section 713(e) eliminates earnings for the lowest year from the "standard of normal earnings", and substitutes 75% of the earnings for the three higher years in their place. This computation of the statutory standard is sometimes called the "75% rule". The effect of Stimson's strike in 1937 was to cause the above standard of normal earnings to be inadequate because of two factors: (1) the figure used for 1937 earnings was too low; (2) the substituted figure for 1938 earnings (being based in part on such low 1937 earnings) was also too low.

The methods of computing the *constructive* average base period net income by use of the reconstructed figure for 1937, as claimed by the Commissioner and Stimson, respectively (R. 15, 16, 18, 19), compare as follows:

Year	Commissioner Ordinary Arithmetic Average	Stimson Constructive Standard of Normal Earnings
1936	$ 89,422.67	$ 89,422.67
1937 (reconstructed)	85,263.34	85,263.34
1938	38,127.75	.....
1939	111,839.77	111,839.77
Aggregate	$324,653.53	$286,525.78
Average	$ 81,163.38	$ 95,508.59
Substitute 75% of 3-year average for 1938		$ 71,631.44
Aggregate for 1936, 1937 and 1939, as above		286,525.78
Aggregate for four years		$358,157.22
Average		$ 89,539.31
Excess profits credit (95%)	$ 77,105.21	$ 85,062.34

Computing "*constructive* average base period net income" as Stimson contends in the manner prescribed by the definition in section 713(e), corrects the two abnormally low factors above mentioned, namely, (1) the low earnings for 1937, and (2) the low substituted figure for 1938 based in part on 1937 earnings. The result is a constructive statutory standard of $89,539.31, (which approximately equals actual earnings for 1936) and an excess profits credit computed at 95% thereof amounting to $85,062.34.

The Commissioner's method of computing the "constructive average base period net income" as required by his regulations (see appendix) not only fails to correct the statutory factor for the year 1938, but uses $38 127.75, a lower figure for that year, than the substituted figure of $66,242.25 which the statute required to be used before "relief" was granted. According to the Commissioner the result is a "constructive average base period net income" of $81,163.38, and an excess profits credit of 95% or $77,105.21 (which is less than the "average" of $82,802.82 and the credit of $78,662.68, before "relief" was granted).

The Commissioner held that the average shall be the amount of $82,802.82 computed under section 713(e) before "relief" was granted (R. 15, 16). The Court of Appeals and the Tax Court by their decisions herein have affirmed the action of the Commissioner.

Before the application of relief provisions the amount of tax paid by Stimson for the year 1942 (R. 11, 12) was as follows:

	Earnings Year 1942	Tax Thereon Rate	Tax Thereon Amount
Subject to Income Tax	$ 83,743.50	40%	$ 33,497.40
Subject to Excess Profits Tax	279,298.24	90%	251,368.42
Total	$363,415.74	78%	$284,865.82

If Stimson's claims respecting the proper computation of the constructive average are sustained, the excess profits credit will be increased from $78,662.68 to $85,062.35 — an increase of $6,399.67. The tax reduction (which would be subject to adjustment for the post-war credit) would be computed as follows:

	Difference in E. P. Credit	Tax Rate	Thereon Amount
Decrease in income subject to excess profits tax	$6,399.67	90%	$5,759.70
Increase in income subject to income tax	6,399.67	40%	2,559.87
Net reduction in total tax			$3,199.83

Similar relief may also be applicable to petitioner's subsequent excess profits tax years not involved in this proceeding.

Although Stimson originally asked for greater relief than that given by the Commissioner's discretionary determination of normal earnings in the amount of $85,263.34 for the year 1937, Stimson raises no question with respect to that determination.

The only issue is whether the Commissioner may require Stimson to use a constructive average base period net income not in accordance with the definition of "average base period net income" in section 713(d) and (e). Stimson's average base period net income computed without using reconstructed earnings for 1937 has been shown to be an inadequate standard of normal earnings and the statute deems the resulting excess profits tax to be excessive and discriminatory. Concededly, Stimson has borne the burden of establishing everything that was required to be established by section 722 in order to obtain relief. Concededly, if there had been no strike to reduce peti-

tioner's earnings below $85,263.34 for the year 1937, the statute would have required the average to be computed at $89,539.31 and the excess profits credit, at $85,062.34. The issue, then, is whether the relief to which Stimson has proved it is entitled, may, nevertheless, be denied by the Commissioner's requirement that reconstructed normal earnings for one or more of the base period years may not be averaged in accordance with the standard that is concededly applicable in averaging normal earnings.

II. Statement particularly disclosing basis of jurisdiction.

The jurisdiction of this Court is invoked under section 240(a) of the Judicial Code, 28 U.S.C.A. Sec. 347(a), providing "in any case, civil or criminal, in a Circuit Court of Appeals, . . . it shall be competent for the Supreme Court of the United States, upon the petition of any party thereto, . . . to require by certiorari . . . that the cause be certified to the Supreme Court . . ."

The date of the judgment of the Circuit Court of Appeals herein sought to be reviewed was July 21, 1947 (R. 81), and Stimson's petition for rehearing which was timely filed was denied on August 25, 1947 (R. 82).

Stimson avers that section 732(c) of the Internal Revenue Code (26 U.S.C.A. Sec. 732(c)), providing "If in the determination of the tax liability under this subchapter the determination of any question is necessary solely by reason of . . . section 722, the determination of such question shall not be reviewed or re-determined by any court or agency except the Board" (now the Tax Court), does not affect the jurisdiction of this Court for the following alternative reasons:

1. A determination respecting the computation of a constructive "average base period net income" involves

the construction of sections 713 and 722 and therefore is not the determination of a question necessary solely by reason of section 722. The Court of Appeals held (R. 70) that section 732(c) did not affect its jurisdiction because the determination of the question herein was necessary by reason of both sections.

2. Section 722 imposes a ministerial duty on the Commissioner to compute the "constructive average base period net income" as required by the statute, and the Commissioner has no discretionary power to "determine" whether to obey or disobey that duty, nor has he jurisdiction to make any "determination" relating thereto the review of which is precluded by section 732(c).

3. The Commissioner in prescribing rules for such constructive average, has attempted to make a "determination" which is beyond and outside of the statutory standards and provisions limiting the discretionary jurisdiction which Congress has conferred upon him, and such attempted "determination" is a nullity and does not constitute a determination the review of which is barred by section 732(c).

III. The questions presented.

Question 1. Whether the jurisdiction of this Court to review the decision of the Court of Appeals is affected by section 732(c) (since this Court has the right and duty to determine its own jurisdiction).

Question 2. Whether the proper construction of the statute requires that "constructive average base period net income" be computed by using reconstructed normal earnings "in one or more taxable years in the base period" in the manner provided in section 713(e) as though such

earnings were the "excess profits net income" for the year or years for which such earnings are established.

Question 3. Whether Congress delegated, or under the Constitution could delegate, to the Commissioner, a discretionary power legislative in its nature, to determine what should constitute a "constructive average base period net income".

Question 4. Whether the computation of the constructive average is the statutory command which Congress has authorized to become operative upon the ascertainment of a basic conclusion of fact, namely the ascertainment of "a fair and just amount representing normal earnings".

Question 5. Whether the Commissioner's discretion ends with the determination of a fair and just amount representing normal earnings. and the remaining duty to compute the "constructive average base period net income" is only a purely ministerial duty.

Question 6. Whether the Commissioner in prescribing regulations which are contrary to the definition of "average base period net income" has exceeded his jurisdiction and attempted to exercise a pretended power beyond and outside of the limits fixed by statute for the exercise of the granted power.

Question 7. Whether regulations of the Commissioner are valid in providing that the "constructive average is a fair and just amount representing normal earnings" and that in computing the constructive average "a taxpayer is not entitled to use the rules provided by section 713(e)(1)".

Question 8. Whether the statutory authority to establish "a fair and just amount representing *normal earnings*" can be extended by the Commissioner to mean a fair and just amount representing a *constructive average*.

Question 9. Whether the Commissioner may deny the use of the 75% rule of section 713(e) in computing constructive average base period net income on the theory that the use of the 75% rule does not result in a fair and just amount.

Question 10. Whether the provisions of section 713(e) prevent the use of the formula prescribed by that section in determining the amount of the constructive average base period net income.

Question 11. Whether subsections (b) and (c) of section 722 in effect provide that a taxpayer is entitled to use section 713 after qualifying for relief, and if so whether the expression "constructive average base period net income" in section 722(a) should accordingly be construed with the definition of "average base period net income" in section 713.

Question 12. Whether the expression "constructive average base period net income" in subsection 722(a) is *in pari materia* with, and should be construed with, the definition of "average base period net income" in section 713.

Question 13. Whether the computation of the constructive average in the manner provided by section 713(e) as was clearly required by the 1941 enactment of section 722, was changed or intended to be changed by the language of section 722 as enacted in 1942.

Question 14. Whether the requirement of section 722(a) that the constructive average be used "in lieu of" the average determined under section 713(e) prevents the "constructive average base period net income" from being computed in the manner provided in section 713(e).

Question 15. Whether Regulations 112, Section 35.722-2 and other regulations which relate to the computation of

the constructive average, are invalid as a whole, or in part.

Question 16. Whether under the stipulation herein Stimson is entitled to have the figure for the year 1938 adjusted pursuant to the 75% rule of section 713(e) in using reconstructed 1937 earnings in the computation of the constructive average base period net income.

Question 17. Whether the expression "constructive average base period net income" should be construed so that section 722 might give the relief it was intended to provide.

IV. Reasons for allowance of the writ.

1. The Court of Appeals, in sustaining the Commissioner's assumption of power to determine the rules governing himself in the computation of the constructive average which rules have the effect of nullifying all or part of the excess profits tax relief to which thousands of taxpayers should be entitled after full compliance with all statutory requirements for obtaining such relief, has decided an important question relating to the construction of sections 713 and 722 of the Internal Revenue Code. Applications for such relief have been filed by approximately 17,600 corporations, and it is estimated that the total refunds of excess profits taxes to be claimed when all such applications shall have been filed will aggregate eight billion dollars.[4] Whether the Commissioner has the power thus to depart from the statutory definition of "average base period net income" in computing a "con-

[4] Commissioner's Statement on the Administration of Section 722, for the Joint Committee on Internal Revenue Taxation, January 18, 1946, as reported by Commerce Clearing House, Volume 3A for 1946, paragraph 5607.05, page 9317.

structive average base period net income", has not been, but should be, settled by this Court.

2. The decision of the Court of Appeals, in sustaining the Commissioner's assumption of power to determine the rules governing himself in the computation of the constructive average and in holding (R. 72) that " 'constructive average base period net income' is established by the discretionary use of rules and methods," is probably in conflict with principles of administrative law laid down and applied in the following:

Addison v. *Holly Hill Fruit Products, Inc.*, 1944, 322 U. S. 607, 616, 88 L. ed. 1488, 1495.

Waite v. *Macy*, 1918, 246 U. S. 606, 608, 609, 62 L. ed. 892, 894.

Lukens Steel Co. v. *Perkins*, 1939, Court of Appeals, Dist. of Col., 107 F. 2d 627, 630.

3. In treating the computation of the constructive average as though it were the ascertainment of a basic conclusion of fact by an administrative officer, rather than the statutory command which becomes operative when the Commissioner has determined as a basic conclusion of fact the "fair and just amount representing normal earnings to be used as" that average, the decision of the Court of Appeals is probably in conflict with the principles respecting the delegation of discretionary authority to administrative officers laid down by this Court in the following cases:

Opp Cotton Mills v. *Administrator*, 1941, 312 U. S. 126, 145, 85 L. ed. 624, 636.

Hirabayashi v. *United States*, 1943, 320 U. S. 81, 104, 87 L. ed. 1774, 1788.

Yakus v. *United States*, 1944, 321 U. S. 414, 424, 425, 88 L. ed. 834, 848.

Bowles v. *Willingham*, 1944, 321 U. S. 503, 515, 88 L. ed. 892, 903, 904.

4. In failing to hold that the computation of the constructive average is only a purely ministerial duty, the decision of the Court of Appeals is also probably in conflict with principles of administrative law laid down in the following:

Roberts v. *United States ex rel Valentine*, 1900, 176 U. S. 219, 231, 44 L. ed. 443, 447.

Butterworth v. *Hoe*, 1884, 112 U. S. 50, 68, 28 L. ed. 656, 662.

Kendall v. *Stokes*, 1838, 12 Peters (37 U. S.) 524, 614, 9 L. ed. 1181, 1216.

Miller v. *Black*, 1888, 128 U. S. 40, 52, 32 L. ed. 354, 358.

United States v. *Hines*, 1939, Court of Appeals, Dist. of Col., 103 F. 2d, 737, 745.

Blair, Commissioner v. *Birkenstock*, 1925, Court of Appeals, Dist. of Col., 6 F. 2d 679, 681.

Blair, Commissioner v. *Union Pac. R. Co.*, 1925, Court of Appeals, Dist. of Col., 6 F. 2d 484, 486.

5. In failing to hold that the relief provisions of section 722 should be construed to give the relief which Congress intended to provide, the decision of the Court of Appeals is probably in conflict with principles laid down and applied in the following:

United States v. *Ogilvie Hardware Co., Inc.*, April 7, 1947, ... U. S. ....., 47-1 U.S.T.C., paragraph 9209.

Bonwit Teller & Co. v. *United States*, 1931, 283 U. S. 258, 263, 75 L. ed. 1018, 1021.

6. Because of differences in language (R. 77), the Court of Appeals held that the 1942 Act did not provide

for computing the constructive average in the manner provided by section 713(e) as did the 1941 Act. In so holding the Court of Appeals disregarded the substance and effect of the 1942 Act as compared with the 1941 Act, and seems to have so far departed from the accepted and usual principles applicable to the construction of statutes (including the principle of resort to explanatory legislative history as laid down by this Court in *Harrison* v. *Northern Trust Co.*, 1943, 317 U. S. 476, 479, 87 L. ed. 407, 410) as to call for an exercise of this Court's power of supervision.[5]

[5] See point B of argument in accompanying brief.

Prayer for Writ.

Wherefore, petitioner prays that this Court issue a Writ of Certiorari to review the judgment of the United States Circuit Court of Appeals for the Ninth Circuit in the instant case entered July 21, 1947, with respect to which a timely petition for rehearing was denied August 25, 1947.

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IN THE

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OCTOBER TERM, 1947.

No. _____

STIMSON MILL COMPANY,
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vs.

COMMISSIONER OF INTERNAL REVENUE,
Respondent.

BRIEF IN SUPPORT OF PETITION FOR A WRIT OF CERTIORARI.

Opinions Below.

The opinion of the Circuit Court of Appeals (July 21, 1947) is reported at ..... F. 2d ..... It is printed in full in the Transcript of the Record (at pages 62 to 80, inclusive).

The opinion of the Tax Court (October 31, 1946) is reported at 7 T. C. 1065. It is printed in full in the Transcript of the Record (at pages 21 to 40, inclusive).

Jurisdiction.

The grounds upon which the jurisdiction of this Court is invoked are stated under division II at pages 7 and 8 of the foregoing petition.

Statement of the Case.

A statement of the case is set forth under division I at pages 1 to 7 of the preceding petition, and the same is hereby adopted and made a part of this brief.

Specification of Errors.

Errors intended to be urged are those specified as questions 2 to 17, inclusive, under division III of the petition at pages 8 to 11, the Court of Appeals having ruled adversely to Stimson or having failed to rule on such questions.

Summary of Argument.

A. Discretionary power of the Commissioner to determine "normal earnings" does not extend to prescribing rules for the computation of a constructive average base period net income differing from the applicable statutory definition. (Reasons 2, 3 and 4 for allowance of the writ.)

B. Provisions in the 1941 Act parallel to those in the 1942 Act require that the constructive average be computed in the manner provided by section 713, and such provisions were not changed in substance or effect by changes in language in the 1942 Act. (Reason 6 for allowance of the writ.)

C. Although Stimson's tax admittedly is excessive and discriminatory and although full proof has been made entitling Stimson to relief, nevertheless relief has been denied in disregard of principles of statutory construction laid down and applied by this Court in other cases. (Reason 5 for allowance of the writ.)

Argument.

A. Discretionary power of the Commissioner to determine "normal earnings," does not extend to prescribing rules for the computation of a constructive average base period net income differing from the applicable statutory definition.

The Commissioner has assumed power to prescribe that when section 722 is applied, the "*constructive*[1] average base period net income" shall be an ordinary arithmetic average instead of an "average base period net income" constructed by using normal earnings in the manner provided by section 713.[2]

It is submitted that the word, "constructive",[3] does not bestow such power on the Commissioner. While a "constructive" result is one that is built upon a certain assump-

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[1] Emphasis throughout this brief, by use of italics, is supplied by petitioner.

[2] Pertinent provisions of sections 713 and 722 and of the regulations are set forth in the appendix.

[3] Definition of "Constructive":

"Deduced by construction or interpretation; resulting from a certain interpretation; not directly expressed but inferred; inferential, virtual; often applied in legal language to what in the eye of the law amounts to the act or condition specified." A New English Dictionary on Historical Principles, by J. A. H. Murray, Vol. II, Part II, page 881, Oxford, 1893.

"Derived from, or depending on, construction or interpretation; not directly expressed, but inferred;—often applied in law to an act or condition assumed from other acts or conditions which are considered (either as an inference or from public policy) as amounting to or involving the act or condition assumed, as in **constructive** fraud, notice, total loss, trust, etc. * * *"—Webster's New International Dictionary, Second Edition.

"That which amounts in the view of the law to an act, although the act itself is not necessarily really performed." Bouvier's Law Dictionary, 1897.

tion or assumptions, nevertheless, that result must have a close resemblance or similitude to the thing it represents by construction, so that in the view of the law it can reasonably amount to the thing itself which is thereby constructed.

Constructive receipt occurs where the assumed element is the clipping and cashing of coupons on bonds in the place of the actual element of clipping and cashing such coupons, and where the remaining actual elements — ownership of the bonds, maturity of the interest coupons, and ability of the issuer to pay — are the same as in actual receipt.[4] Similarly, a *constructive* "average base period net income" must be based on an assumed element which replaces an actual element and is combined with remaining actual elements in the formula for an "average base period net income."

The statute does not leave to official discretion the assumption which is to be made for a "constructive average." Section 722(a) specifies "a fair and just amount representing normal earnings to be used as a constructive average base period net income." The Commissioner has discretion to determine "normal earnings." But the constructive average is to be computed by using such "normal earnings" in the place of an actual element in the formula therefor. Since the formula of Section 713(e) provides for using "excess profits net income for each of the taxable years of the taxpayer in the base period," it is obvious that "excess profits net income" is the element in the formula to be replaced by "normal earnings."

Section 722(b) (1), here applicable, provides for relief

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[4] Merten's Law of Federal Income Taxation, Vol. 2, section 10.12, p. 19. See also Id., Vol. 2, page 1, et seq., for other examples of constructive receipt.

from the effects of abnormalities "in one or more taxable years of the base period." Consequently, "normal earnings", established for Stimson for the year 1937, are to be substituted for "excess profits net income" for that year in the computation of the 75% rule, and the adjustment of the figure for 1938 to $71,631.44 must follow as a matter of statutory requirement.

> "When a statute limits a thing to be done in a particular mode, it includes the negative of any other mode." *Botany Worsted Mills* v. *United States,* 1928, 278 U. S. 282, 289, 73 L. ed. 379, 385.

Any alleged discretionary power of the Commissioner with respect to computing a constructive average, is bounded and limited by the specific statutory details outlined above, so that the Commissioner's action in prescribing contrary rules is a nullity — a mere attempted exercise of discretionary power beyond and outside of the statutory boundaries limiting his jurisdiction.

In sustaining the rent control provisions of the Emergency Price Control Act of 1942, this Court summarized the applicable administrative principles by stating:

> "Congress here has specified the basic conclusions of fact upon the ascertainment of which by the administrator its statutory command is to become effective." *Bowles* v. *Willingham,* 1944, 321 U. S. 503, 515, 88 L. ed. 892, 903, 904.

The computation of the constructive average in the case at bar clearly appears to be — not "the ascertainment of a basic conclusion of fact" by the Commissioner, but — the statutory command which becomes effective upon the ascertainment of the fair and just amount representing normal earnings.

In holding invalid a regulation of the Administrator under the Fair Labor Standards Act, this Court reviewed

a situation which seems to be akin to that in the instant case, saying:

> "In any event, Congress did not leave it to the Administrator to decide whether within geographic bounds defined by him the Act further permits discrimination between establishment and establishment based upon the number of employees. *The determination of the extent of authority given to a delegated agency by Congress is not left for the decision of him in whom authority is vested.* . . . The details with which the exemptions in this Act have been made preclude their enlargement by implication. . . . Construction is not legislation and must avoid 'that retrospective expansion of meaning which properly deserves the stigma of judicial legislation.'" *Addison* v. *Holly Hill Fruit Products,* 1944, 322 U. S. 607, 616, 618, 88 L. ed. 1488, 1495, 1496.

For the reasons stated above it is respectfully submitted that the decision of the Court of Appeals is contrary to principles laid down and applied in decisions of this Court cited in reasons numbered 2, 3 and 4 in the Reasons For Allowance of the Writ set forth in the Petition.

B. Provisions in the 1941 Act parallel to those in the 1942 Act, required that the constructive average be computed in the manner provided by section 713, and such provisions were not changed in substance or effect by changes in language in the 1942 Act.

The Committee on Ways and Means in Report No. 2333 accompanying the Revenue Bill of 1942 reiterated *the same purpose* which had motivated Congress in providing for excess profits tax relief in the years 1940 and 1941. The report[6] states:

> "The need for this legislation was recognized when

[6] As reported in Internal Revenue Bulletin—Cumulative Bulletin 1942-2, at page 390.

> the excess-profits tax was enacted in 1940, and in the excess-profits tax amendments of 1941, as pointed out in the committee reports on those Acts. . . . It was there stated that equitable considerations demand that every reasonable precaution should be taken to prevent unfair application of the excess-profits tax in abnormal cases; . . . The rates now proposed increase the need for expanding the application of the relief section to cases that do not fall under the specific provisions in order to remove inequities and alleviate certain hardships."

Since the same legislative purpose motivated the 1941 enactment of section 722 as motivated the 1942 enactment of that section, provisions of the 1941 Act may be considered in interpreting parallel provisions of the 1942 Act. The pertinent provisions of both Acts are shown in the appendix.

The 1941 Act (in section 722(b) (3)) specifically required that the constructive average be computed in the same manner as provided in section 713(d) which in turn requires use of subsections (e) and (f). In 1942 there was no need of referring specifically to the provisions of section 713(d) because the term "constructive average base period net income" includes the term "average base period net income" which is the title of the subject matter covered in section 713(d) and the designation of such title is itself a specific reference to section 713(d). Thus in both the 1941 Act and the 1942 Act the redetermined earnings for the years of the base period are substituted for "excess profits net income" in making the computation in the manner provided by section 713(d) — which in turn specifies the use of section 713(e) here applicable.

Contrary to the holding by the Court of Appeals (R. 77), in substance and effect the 1942 version of section 722 therefore did *not* omit the provision of the 1941 Act that

the constructive average be computed as in section 713. Similarly, the other of the changes in language in the 1942 Act cited by the Court of Appeals as "a drastic alteration of the law", namely that the 1942 Act "required a 'constructive average' to be used 'in lieu of' the section 713 average", is in fact no change whatever in substance and effect. Section 722(a) of the 1941 Act provided that "the amount established under paragraph (3) shall be considered as the average base period net income of the taxpayer for the purposes of this subchapter." By that language the 1941 Act requires exactly the same result as does the 1942 Act, namely that the constructive average (computed in the manner provided by section 713) be used in lieu of the section 713 average for the computation of the excess profits credit and the excess profits tax.

The Court of Appeals (R. 78) refused the aid of reports of Congressional committees which support the natural interpretation of the two Acts we have set forth above, and we submit that in so doing the Court of Appeals has held contrary to the principles laid down by this Court in *Harrison* v. *Northern Trust Co.*, 1943, 317 U. S. 476, 479, 87 L. ed. 407, 410, where this Court stated:

> "But words are inexact tools at best and for that reason there is wisely no rule of law forbidding resort to explanatory legislative history no matter how 'clear the words may appear on "superficial examination" '. *United States* v. *American Trucking Assn.*, 310 U. S. 534, 543, 544, 84 L. ed. 1345, 1350, 1351. See also *United States* v. *Dickerson*, 310 U. S. 554, 562, 84 L. ed. 1356, 1362."

It is submitted that the decision of the Court of Appeals disregards the substance of the 1942 Act as compared with the substance of the 1941 Act, and has so far departed from the accepted and usual principles applicable to the

construction of statutes as to call for an exercise of this Court's power of supervision.

C. Although Stimson's tax admittedly is excessive and discriminatory and although full proof has been made entitling Stimson to relief, nevertheless relief has been denied in disregard of principles of statutory construction laid down and applied by this Court in other cases.

In its opinion the Court of Appeals states (R. 78):

> "Fourth: Taxpayer argues that since it has established both conditions precedent for the use of section 722, the tax must be determined by the constructive average. With this we agree."

The two conditions precedent for obtaining relief are:

1. That the tax is excessive and discriminatory.
2. What would be a fair and just amount representing normal earnings.

As a result of Stimson's proof of the effect of the strike on 1937 earnings, it follows under section 722(b) that the tax "shall be considered to be excessive and discriminatory" for the reason that Stimson's "average base period net income is an inadequate standard of normal earnings."

The average which Stimson has thus proven to be an inadequate standard is computed on the following elements required by the statute:

1. 1936 excess profits net income	$ 89,422.67
2. 1937 excess profits net income	63,706.57
3. 1938—75% of average for other three years	66,242.25
4. 1939 excess profits net income	111,839.77
Inadequate average (without benefit of relief)	$ 82,802.82

Stimson also established that $85,263.34 represented the corrected normal earnings for the year 1937. Both parties agree that such $85,263.34 should replace the 1937 figure of $63,706.57 in computing the constructive average.

They disagree, however, as to what should be done with the figure of $66,242.25 for 1938. The Commissioner claims that this figure should be reduced to $38,127.75, the "excess profits net income" for that year. Stimson claims the figure of $66,242.25 should be increased to $71,631.44 pursuant to the 75% rule after 1937 earnings are corrected.

Inasmuch as the above average has been proven to be inadequate, and inasmuch as the purpose of Congress in enacting this relief measure was clearly to make adequate such an inadequate average, it appears unreasonable, if not absurd, that the Commissioner should pretend to comply with the relief provisions by *reducing* a figure on which the average is computed. He might more plausibly contend that the 1938 figure should remain at $66,242.25 in the constructive average. It is submitted, however, that section 722(a) clearly requires corrected "normal earnings" to be used in the manner provided by the formula of section 713(e), with a resulting figure of $71,631.44 for 1938 and a constructive average amounting to $89,539.31.

According to the Commissioner, the constructive average turns out to be less than the inadequate average of $82,802.82 determined before relief was granted, with the result that relief must be denied. Stimson is left with the inadequate average of $82,802.82 and the excessive and discriminatory tax based thereon. The relief provisions are thus interpreted as a futile Congressional gesture, and Stimson, having concededly complied with all statutory requirements to obtain relief, is nevertheless deprived of relief from a tax which section 722(b) declares to be excessive and discriminatory.

This Court has held that statutes should be construed to give the relief which Congress intended to provide. In *Bowit Teller & Co.* v. *United States,* 1931, 283 U. S. 258, 263, 75 L. ed. 1018, 1021, this Court stated the principle involved:

> "The section is a part of a tax law giving to taxpayers opportunity to secure a refund of overpayments that had become barred. Manifestly, it is to be construed liberally in favor of the taxpayers to give the relief it was intended to provide."

This Court allowed the relief which Congress intended to provide in construing another relief amendment of the 1942 Act authorizing corporations to obtain refunds of undistributed profits tax, in *United States* v. *Ogilvie Hardware Co., Inc.,* ..... U. S. ....., decided April 7, 1947 (47-1 U.S.T.C., paragraph 9209), in which this Court said:

> "The language of this extraordinary relief measure and the circumstances which prompted its passage convince us that Congress intended to provide refunds to corporate taxpayers. . . . In order that this purpose may be effected, the judgment of the Circuit Court of Appeals is affirmed."

It is submitted that sections 713 and 722 not only can, but should, be construed to provide the relief intended, and that in failing to so construe these sections the decision of the Court of Appeals is in conflict with the principles laid down and applied in the cases just cited.

It is respectfully submitted that the prayer of the foregoing petition should be granted.

Bert L. Klooster

BERT L. KLOOSTER,
Attorney for Petitioner.

CHAPMAN AND CUTLER,
Of Counsel.

APPENDIX

Excerpts from
Sections 712 and 713 of the Internal Revenue Code as amended[1] (Title 26, U.S.C.A., Sections 712 and 713).

SUBCHAPTER E—EXCESS PROFITS TAX
PART I

* * * * * *

§712. EXCESS PROFITS CREDIT—ALLOWANCE

(a) DOMESTIC CORPORATIONS.—In the case of a domestic corporation which was in existence before January 1, 1940, the excess profits credit for any taxable year shall, at the election of the taxpayer made in its return for such taxable year, be an amount computed under section 713 or section 714, whichever amount results in the lesser tax under this subchapter for the taxable year for which the tax under this subchapter is being computed . . . .

* * * * * *

§713. Excess profits credit—Based on income.

(a) Amount of excess profits credit. The excess profits credit for any taxable year, computed under this section, shall be—

(1) Domestic corporations. In the case of a domestic corporation—

(A) 95 per centum of the average base period net income,

* * * * * *

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[1] Pursuant to Section 122(a) of the Revenue Act of 1945, the excess profits tax provisions of subchapter E of chapter 2 of the Internal Revenue Code "shall not apply to any taxable year beginning after December 31, 1945," 26 U.S.C.A. Internal Revenue Acts beginning 1940, p. 573.

(b) Base Period.

(1) Definition. As used in this section the term "base period"—

(A) If the corporation was in existence during the whole of the forty-eight months preceding the beginning of its first taxable year under this subchapter, means the period commencing with the beginning of its first taxable year beginning after December 31, 1935, and ending with the close of its last taxable year beginning before January 1, 1940; and

* * * * * *

(d) Average base period net income—determination.

(1) Definition. For the purposes of this section the average base period net income of the taxpayer shall be the amount determined under subsection (e), subject to the exception that if the aggregate excess profits net income for the last half of its base period, reduced by the aggregate of the deficits in excess profits net income for such half, is greater than such aggregate so reduced for the first half, then the average base period net income shall be the amount determined under subsection (f), if greater than the amount determined under subsection (e).

* * * * * *

(e) Average base period net income—general average. The average base period net income determined under this subsection shall be determined as follows:

(1) By computing the aggregate of the excess profits net income for each of the taxable years of the taxpayer in the base period, reduced by the sum of the deficits in excess profits net income for each of such years. If the excess profits net income (or deficit in excess profits net income) for one taxable year in the base period divided by the number of months in such taxable year is less than 75 per centum of the aggregate of the excess profits net income (reduced by deficits in excess profits net income) for the other tax-

able years in the taxpayer's base period divided by the number of months in such other taxable years (herein called "average monthly amount") the amount used for such one year under this paragraph shall be 75 per centum of the average monthly amount multiplied by the number of months in such one year, and the year increased under this sentence shall be the year the increase in which will produce the highest average base period net income;

(2) By dividing the amount ascertained under paragraph (1) by the total number of months in all such taxable years; and

(3) By multiplying the amount ascertained under paragraph (2) by twelve.[2]

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[2] Section 713(e)(1) was amended to the language above-quoted by section 215 of the Revenue Act of 1942, 26 U.S.C.A. Internal Revenue Acts beginning 1940, p. 292, effective for the year 1942. Previously section 713(e)(1) provided the "deficit rule" reading as follows:

> (1) By computing the aggregate of the excess profits net income for each of the taxable years of the taxpayer in the base period, reduced, if for more than one of such taxable years there was a deficit in excess profits net income, by the sum of such deficits, excluding the greatest;

The deficit rule, just quoted, was provided by Section 4(a), Excess Profits Tax Amendments of 1941 (26 U.S.C.A. Internal Revenue Acts Beginning 1940, p. 79).

Excerpts from
Section 722 of the Internal Revenue Code (26 U.S.C.A. Sec. 722).[3]

§722. General relief—Constructive average base period net income;

(a) *General rule.* In any case in which the taxpayer establishes that the tax computed under this subchapter (without the benefit of this section) results in an excessive and discriminatory tax and establishes what would be a fair and just amount representing normal earnings to be used as a constructive average base period net income for the purposes of an excess profits tax based upon a comparison of normal earnings and earnings during an excess profits tax period, the tax shall be determined by using such constructive average base period net income in lieu of the average base period net income otherwise determined under this subchapter. In determining such constructive average base period net income, no regard shall be had to events or conditions affecting the taxpayer, the industry of which it is a member, or taxpayers generally occurring or existing after December 31, 1939, except that, in the cases described in the last sentence of section 722 (b) (4) and in section 722 (c), regard shall be had to the change in the character of the business under section 722 (b) (4) or the nature of the taxpayer and the character of its business under section 722 (c) to the extent necessary to establish the normal earnings to be used as the constructive average base period net income.

(b) Taxpayers using average earnings method. The tax

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[3] As amended by the Revenue Act of 1942, Section 222 (26 U.S.C.A. Internal Revenue Acts beginning 1940, pp. 297, 298, 299), effective for the year 1942, the year in question herein.

computed under this subchapter (without the benefit of this section) shall be considered to be excessive and discriminatory in the case of a taxpayer entitled to use the excess profits credit based on income pursuant to section 713, if its average base period net income is an inadequate standard of normal earnings because—

(1) in one or more taxable years in the base period normal production, output, or operation was interrupted or diminished because of the occurrence, either immediately prior to, or during the base period, of events unusual and peculiar in the experience of such taxpayer,

(2) the business of the taxpayer was depressed in the base period because of temporary economic circumstances unusual in the case of such taxpayer or because of the fact that an industry of which such taxpayer was a member was depressed by reason of temporary economic events unusual in the case of such industry,

• • • • • •

Excerpts from
Section 722 (1941 Act) of the Internal Revenue Code as enacted by Section 6, Excess Profits Tax Amendments of 1941 (26 U.S.C.A. Internal Revenue Acts beginning 1940, pp. 83, 84).

§722. ADJUSTMENT OF ABNORMAL BASE PERIOD NET INCOME

(a) GENERAL RULE.—In the case of a taxpayer whose first taxable year under this subchapter begins in 1940, if the taxpayer establishes—

(1) that the character of the business engaged in by the taxpayer as of January 1, 1940, is different from the character of the business engaged in during one or more of the taxable years in its base period (as defined in section 713 (b) (1)); or

(2) that in one or more of the taxable years in such base period normal production, output, or operation was interrupted or diminished because of the occurrence of events abnormal in the case of such taxpayer; and

(3) the amount that would have been its average base period net income—

(A) if the character of the business as of January 1, 1940, had been the same during each of the taxable years of such base period; and

(B) if none of the abnormal events referred to in paragraph (2) had occurred; and

(C) if in each of such taxable years none of the items of gross income had been abnormally large, and none of the items of deductions had been abnormally small; and

(4) that the amount established under paragraph (3) is greater than the average base period net income computed under section 713 (d) or section 742, as the case may be,

then the amount established under paragraph (3) shall be considered as the average base period net income of the taxpayer for the purposes of this subchapter.

(b) RULES FOR APPLICATION OF SUBSECTION (a). For the purposes of subsection (a)—

* * * * * *

(3) The average base period net income determined under subsection (a) (3) shall be computed in the same manner as provided in section 713 (d), except paragraphs (2) and (4), but for such purposes computing excess profits net income and deficit in excess profits net income on the basis of the assumptions made in subsection (a) (3).

(4) If subsection (a) (1), or both subsections (a) (1) and (a) (2) are applicable to any taxpayer, its average base period net income under subsection (a) (3) shall not exceed the excess profits net income (as computed for the purposes of subsection (a) (3), for the last taxable year in such base period. . . . . .

Excerpt from
Regulations 112, Section 35.722-2(b).

(1) Section 722(a) provides for the determination of a constructive average base period net income to be used in lieu of the actual average base period net income in those cases to which section 722 is applicable. Therefore, in computing such amount a taxpayer is not entitled to use the rules provided by section 713 (e) (1), relating to increase in base period net income of lowest year of base period, or by section 713 (f), relating to average base period net income in case of increased earnings in last half of base period. Since the constructive average base period net income is the fair and just amount representing normal earnings and will reflect adjustments for abnormally low base period years, a taxpayer having computed such amount is not entitled in addition to apply the rules provided by section 713(e) (1). In a proper case, however, growth may be recognized in arriving at the fair and just amount representing normal earnings if, and to the extent that, such recognition is reasonable and consistent with the conditions and limitations of section 722.

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CITATIONS

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In the Supreme Court of the United States

OCTOBER TERM, 1947

No. 395

STIMSON MILL COMPANY, A CORPORATION,
PETITIONER

v.

COMMISSIONER OF INTERNAL REVENUE

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE NINTH CIRCUIT

BRIEF FOR THE RESPONDENT IN OPPOSITION

OPINIONS BELOW

The findings of fact and opinion of the Tax Court (R. 21–40) are reported in 7 T. C. 1065. The opinion of the Circuit Court of Appeals for the Ninth Circuit (R. 61–80) is reported in 163 F. 2d 269.

JURISDICTION

The judgment of the Circuit Court of Appeals was entered July 21, 1947. (R. 81.) The petition for a writ of certiorari was filed October 13,

1947. The jurisdiction of this Court is invoked under Section 240 (a) of the Judicial Code, as amended by the Act of February 13, 1925.

QUESTION PRESENTED

Whether the Circuit Court of Appeals erred in affirming the Tax Court's decision sustaining the Commissioner's denial of the taxpayer's claim for general relief, under Section 722 of the Internal Revenue Code, from the excess profits taxes assessed against it for the taxable year 1942.

STATUTES AND REGULATIONS INVOLVED

The pertinent statute and Treasury Regulations are set out in the Appendix, *infra,* pp. 10–16.

STATEMENT

The Tax Court found the facts as stipulated. (R. 22–27.) These may be summarized as follows: The Commissioner determined an additional excess profits tax liability against the petitioner for the taxable year 1942 in the sum of $2,106.08, making a total tax liability for that year of $251,368.42 (R. 22–23), which the petitioner does not contest, except by reason of its claim that it is entitled to relief therefrom under Section 722 of the Internal Revenue Code, in addition to the benefits provided by Section 713 (e) (1). Accordingly, it was agreed that the proposed deficiency in the amount of $2,106.08 as set forth in the statutory notice of deficiency was

due and had properly been assessed by the Commissioner since the petition for review by the Tax Court was filed by it. (R. 26.)

In determining the excess profits tax liability of the petitioner for the taxable year, the Commissioner computed its excess profits credit, based upon the average base period net income under Section 713 (e) (1). In making such computation, the Commissioner used the petitioner's actual income for the base period years 1936, 1937 and 1939, and 75 percent of the average of those years as its base period net income for its low income year 1938, as required by Section 713 (e) (1). In this manner, the Commissioner computed the petitioner's Section 713 (e) (1) excess profits credit in the sum of $78,662.68. (R. 23–24.)

The petitioner made timely application to the Commissioner for relief under Section 722 from the excess profits tax thus determined, on the form provided therefor, claiming a refund of such tax for 1942. (R. 22.)

The petitioner established by information submitted that its normal operations or output was interrupted in 1937 by strikes or other events peculiar in its experience, of the character provided for by Section 722 (b) (1). It also established that, because of those events, its actual earnings for 1937 in the amount of $63,706.57 were abnormally low. On the basis of the facts

submitted, the fair and just amount representing normal earnings, which would be used by the petitioner as its constructive average base period net income for the year 1937 under the provisions of Section 722 (exclusive of Section 713), was accordingly reconstructed by the Commissioner in the amount of $85,263.34. (R. 24–25.)

In computing the petitioner's excess profits credit under Section 722, the Commissioner used this amount ($85,263.34), as representing the petitioner's normal base period net income for 1937, and its actual net income for the years 1936, 1938 and 1939. The excess profits tax credit thus determined by him under Section 722 was $77,-105.22. (R. 25.)

Since such Section 722 credit (of $77,105.22) was less than the excess profits credit of $78,-662.68 computed under Section 713 (e) (1) (R. 23–24), the Commissioner disallowed the petitioner's claim for Section 722 relief, and notice of such disallowance was issued by him in accordance with the requirements of Section 732. (R. 23.)

The petitioner, on the other hand, contended that it was entitled under the law to compute its excess profits credit for 1942 by reconstruction of its base period net income (for 1937) under Section 722, as above set forth, and also by the application of the provisions of Section 713 (e) (1). This would result in an excess profits credit of $85,062.32, computed by using its actual net

income for the years 1936 and 1939 and its net income as reconstructed under Section 722 (b) (1) for 1937, and by taking 75 percent of the average of these amounts as representing its net income for 1938. (R. 25–26.)

It was further stipulated that, if it was held in accordance with the Commissioner's determination that the petitioner was not entitled to Section 722 relief in addition to the benefits allowed by Section 713 (e) (1), the Tax Court could enter its decision that the petitioner's correct excess profits tax liability for 1942 was the stipulated amount $251,368.42. (R. 26–27.) But, if it was held in accordance with the petitioner's contention that it was entitled to compute its excess profits credit for that year by using both Section 722 and Section 713 (e) (1), then it was agreed that such credit was to be computed in accordance with its contention above set forth and that it had overpaid its excess profits tax for that year in an amount to be determined by the Tax Court under its Rule 50. (R. 27.)

The Tax Court sustained the Commissioner's denial of the petitioner's claim for general relief from the excess profits tax, under Section 722, and the Circuit Court of Appeals affirmed the Tax Court's decision. (R. 80.)

ARGUMENT

1. The petitioner's sole claim is for general relief from the excess profits tax under Section

722 of the Internal Revenue Code (Appendix, *infra,* pp. 11–13). It contends that, in denying such relief, the Commissioner, the Tax Court and the Circuit Court of Appeals erred in misconstruing and misapplying its provisions and, in this connection, that the applicable Treasury Regulations similarly construing the statute are invalid (Treasury Regulations 112, Section 35.722–2, Appendix, *infra,* pp. 14–16). The question thus presented has not been passed on by any other appellate court, and there is thus no conflict of authority. It is submitted that the case is not one calling for review by this Court.

2. There is no proper basis for review, because the question as to the construction and application of Section 722 would, in all probability, not be reached by this Court at all, since the Circuit Court of Appeals was without jurisdiction under Section 732 (c) (Appendix, *infra,* p. 14) to review the Tax Court's decision denying the petitioner Section 722 relief, and this was the only matter before the Circuit Court of Appeals.

In this connection it may be observed that it was stipulated that the excess profits tax in question was properly determined by the Commissioner after allowance of an excess profits credit duly computed under Section 713 (e) (1), as amended by Section 215 of the Revenue Act of 1942 (Appendix, *infra,* pp. 10–11). (R. 26.) It is now well

settled that a claim for refund based on a claim for Section 722 relief cannot, under Section 722 (d) (Appendix, *infra*, p. 13), be filed until the tax shown upon the return has been paid (*Uni-Term Stevedoring Co.* v. *Commissioner*, 3 T. C. 917) or until any deficiency determined by the Commissioner has become final and been assessed and paid. (*American Coast Line* v. *Commissioner*, 159 F. 2d 665 (C. C. A. 2d); *Pohatcong Hosiery Mills, Inc.* v. *Commissioner*, 162 F. 2d 146 (C. C. A. 3d)).

Thus, in this case the petitioner filed its claim for refund only after the Commissioner had determined the amount of the petitioner's excess profits tax for the taxable year in question to be $251,368.42 (R. 22–23), which, as stated, was agreed to be the amount due and properly assessed. (R. 26.)

When, therefore, the Commissioner denied the petitioner's claim, the petitioner appealed under Section 732 to the Tax Court only to review such denial. Subsection (c) of Section 732 (Appendix, *infra*) provides that the decision of the Tax Court on such appeal shall be final in respect of any question the determination of which was necessary solely by reason of Section 722. And, since, as stated, the petitioner did not appeal from the Commissioner's determination of the deficiency in the tax, but only from his denial of its claim to Section 722 relief, the question pre-

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sented both to the Tax Court and to the Circuit Court of Appeals was one necessary solely by reason of Section 722, within the meaning of Section 732 (c). Plainly, therefore, the court below should have dismissed the case for want of jurisdiction. Compare its own prior decision in *James F. Waters, Inc.* v. *Commissioner,* 160 F. 2d 596, which involved the construction and application of Section 721.

3. In any case, the petitioner points to nothing in either Section 713 or Section 722 which justifies a conclusion that it is entitled to a hybrid credit computed under both Section 713 (e) (1) and Section 722. As regards the petitioner's contention that its construction of Section 722 is supported by the provisions of the prior law, particularly Section 722 (b) (3) as amended by Section 6 of the Excess Profits Tax Amendments of 1941, c. 10, 55 Stat. 17, it need only be pointed out that the amendments made by the Revenue Act of 1942 in Section 722, particularly in subsection (e) thereof, relating to the rules for the application of the section, entirely omitted the requirement contained in Section 722 (b) (3), as amended by Section 6 of the Excess Profits Tax Act of 1941, that the constructive average base period net income computed under Section 722 (a) be determined in accordance with the computation of the average base period net income under Section 713. There is nothing in the legis-

lative history which justifies a contrary conclusion. Accordingly, even assuming the Circuit Court of Appeals had jurisdiction to determine the proper construction of Section 722, the construction which it made was correct.

CONCLUSION

For the foregoing reasons, it is respectfully submitted that the petition for certiorari should be denied.

PHILIP B. PERLMAN,
Solicitor General.
THERON LAMAR CAUDLE,
Assistant Attorney General.
HELEN R. CARLOSS,
LEE A. JACKSON,
CARLTON FOX,
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NOVEMBER 1947.

APPENDIX

Internal Revenue Code:

SEC. 713 [as added by the Second Revenue Act of 1940, c. 757, 54 Stat. 974, Sec. 201]. EXCESS PROFITS CREDIT—BASED ON INCOME.

* * * * *

(d) [as amended by the Excess Profits Tax Amendments of 1941, c. 10, 55 Stat. 17, Sec. 4] *Average base period net income—Determination.*—

(1) *Definition.*—For the purposes of this section the average base period net income of the taxpayer shall be the amount determined under subsection (e), subject to the exception that if the aggregate excess profits net income for the last half of its base period, reduced by the aggregate of the deficits in excess profits net income for such half, is greater than such aggregate so reduced for the first half, then the average base period net income shall be the amount determined under subsection (f), if greater than the amount determined under subsection (e).

* * * * *

(e) [as amended by the Revenue Act of 1942, c. 619, 56 Stat. 798, Sec. 215] *Average base period net income—General average.*—The average base period net income determined under this subsection shall be determined as follows:

(1) By computing the aggregate of the excess profits net income for each of the

taxable years of the taxpayer in the base period, reduced by the sum of the deficits in excess profits net income for each of such years. If the excess profits net income (or deficit in excess profits net income) for one taxable year in the base period divided by the number of months in such taxable year is less than 75 per centum of the aggregate of the excess profits net income (reduced by deficits in excess profits net income) for the other taxable years in the taxpayer's base period divided by the number in such other taxable years (herein called "average monthly amount") the amount used for such one year under this paragraph shall be 75 per centum of the average monthly amount multiplied by the number of months in such one year, and the year increased under this sentence shall be the year the increase in which will produce the highest average base period net income;

* * * * *

(26 U. S. C. 1940 ed., Sec. 713.)

SEC. 722 [as added by the Second Revenue Act of 1940, *supra*, Sec. 201]. GENERAL RELIEF—CONSTRUCTIVE AVERAGE BASE PERIOD NET INCOME

(a) [as amended by the Revenue Act of 1942, *supra*, Sec. 222 (a)] *General rule.*—In any case in which the taxpayer establishes that the tax computed under this subchapter (without the benefit of this section) results in an excessive and discriminatory tax and establishes what would be a fair and just amount representing normal earnings to be used as a constructive average base period net income for the purposes of an excess profits tax based upon comparison of normal earnings and earn-

ings during an excess profits tax period, the tax shall be determined by using such constructive average base period net income in lieu of the average base period net income otherwise determined under this subchapter. In determining such constructive average base period net income, no regard shall be had to events or conditions affecting the taxpayer, the industry of which it is a member, or taxpayers generally occurring or existing after December 31, 1939, except that, in the cases described in the last sentence of section 722 (b) (4) and in section 722 (c), regard shall be had to the change in the character of the business under section 722 (b) (4) or the nature of the taxpayer and the character of its business under section 722 (c) to the extent necessary to establish the normal earning to be used as the constructive average base period net income.

(b) [as amended by the Revenue Act of 1942, *supra,* Sec. 222 (a)] *Taxpayers using average earnings method.*—The tax computed under this subchapter (without the benefit of this section) shall be considered to be excessive and discriminatory in the case of a taxpayer entitled to use the excess profits credit based on income pursuant to section 713, if its average base period net income is an inadequate standard of normal earnings because—

(1) in one or more taxable years in the base period normal production, output, or operation was interrupted or diminished because of the occurrence, either immediately prior to, or during the base period, of events unusual and peculiar in the experience of such taxpayer,

* * * * *

(d) [as amended by the Act of December 17, 1943, 346, 57 Stat. 601, Sec. 1] *Application for relief under this section.*—The taxpayer shall compute its tax, file its return, and pay the tax shown on its return under this subchapter without the application of this section, except as provided in section 710 (a) (5). The benefits of this section shall not be allowed unless the taxpayer within the period of time prescribed by section 322 and subject to the limitation as to amount of credit or refund prescribed in such section makes application therefor in accordance with regulations prescribed by the Commissioner with the approval of the Secretary. If a constructive average base period net income has been determined under the provisions of this section for any taxable year, the Commissioner may, by regulations approved by the Secretary, prescribe the extent to which the limitations prescribed by this subsection may be waived for the purpose of determining the tax under this subchapter for a subsequent taxable year.

* * * * *

(26 U. S. C. 1940 ed., Sec. 722.)

SEC. 732 [as added by the Excess Profits Tax Amendments of 1941, c. 10, 55 Stat. 17, Sec. 9]. REVIEW OF ABNORMALITIES BY BOARD OF TAX APPEALS.

(a) *Petition to the Board.*—If a claim for refund of tax under this subchapter for any taxable year is disallowed in whole or in part by the Commissioner, and the disallowance relates to the application of section 711 (b) (1) (H), (I), (J), or (K), section 721, or section 722, relating to abnormalities, the Commissioner shall send notice of such disallowance to the taxpayer

by registered mail. Within ninety days after such notice is mailed (not counting Sunday or a legal holiday in the District of Columbia as the ninetieth day) the taxpayer may file a petition with the Board of Tax Appeals for a redetermination of the tax under this subchapter. If such petition is so filed, such notice of disallowance shall be deemed to be a notice of deficiency for all purposes relating to the assessment and collection of taxes or the refund or credit of overpayments.

* * * * *

(c) *Finality of determination.*—If in the determination of the tax liability under this subchapter the determination of any question is necessary solely by reason of section 711 (b) (1) (H), (I), (J), or (K), section 721, or section 722, the determination of such question shall not be reviewed or redetermined by any court or agency except the Board.

* * * * *

(26 U. S. C. 1940 ed., Sec. 732.)

Treasury Regulations 112 promulgated under the Internal Revenue Code:

SEC. 35.722–2. *Constructive average base period net income.*—

* * * * *

(b) *Rules for determination.*—The determination of the constructive average base period net income must depend in each instance upon the facts and circumstances presented by the taxpayer and upon the provisions of section 722 forming the basis of the taxpayer's contention that its excess profits tax is excessive and discriminatory,

i. e., if the taxpayer is entitled to use the excess profits credit based on income, the reasons why such credit is an inadequate standard of normal earnings, or if the taxpayer is not entitled to use such credit, the reasons why the excess profits credit based on invested capital is an inadequate standard for redetermining excess profits. No single test or standard of universal application can be prescribed pursuant to which every taxpayer must establish the fair and just amount representing normal earnings to be used as its constructive average base period net income. However, the following principles and rules must be observed in every case in which a constructive average base period net income is determined:

(1) [as amended by T. D. 5415, 1944 Cum. Bull. 404, 406, and T. D. 5560, 1947–1 Cum. Bull. 72] Section 722 (a) provides for the determination of a constructive average base period net income to be used in lieu of the actual average base period net income in those cases to which section 722 is applicable. Therefore, in computing such amount a taxpayer is not entitled to use the rules provided by section 713 (e) (1), relating to increase in base period net income of lowest year of base period, or by section 713 (f), relating to average base period net income in case of increased earnings in last half of base period. Since the constructive average base period net income is the fair and just amount representing normal earnings and will reflect adjustments for abnormally low base period years, a taxpayer having computed such amount is not entitled in addition to apply the rules provided by section 713 (e) (1). In a proper case, however, growth may be

recognized in arriving at the fair and just amount representing normal earnings if, and to the extent that, such recognition is reasonable and consistent with the conditions and limitations of section 722.

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FILE COPY

IN THE

Supreme Court of the United States

OCTOBER TERM, A. D. 1947.

No. 395

STIMSON MILL COMPANY, a corporation,
Petitioner.

VS.

COMMISSIONER OF INTERNAL REVENUE,
Respondent.

PETITION FOR REHEARING ON PETITION FOR WRIT OF CERTIORARI.

To the United States Circuit Court of Appeals For the Ninth Circuit.

BERT L. KLOOSTER,
Attorney for Petitioner.

CHAPMAN AND CUTLER,
Of Counsel.

Scheffer Printing Company, Del. 7171

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CERTIFICATE PURSUANT TO RULE 33.

The undersigned, Bert L. Klooster, attorney for Petitioner, hereby certifies that the petition for rehearing filed in this cause is presented in good faith, that in his judgment said petition is restricted to the grounds specified in part 2 of Rule 33 as amended, and that said petition for rehearing is not interposed for delay.

Bert L. Klooster,
Attorney for Petitioner.

IN THE

Supreme Court of the United States

OCTOBER TERM, A. D. 1947.

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STIMSON MILL COMPANY, a corporation,

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PETITION FOR REHEARING ON PETITION FOR WRIT OF CERTIORARI.

To the United States Circuit Court of Appeals For the Ninth Circuit

To the Honorable Fred M. Vinson, Chief Justice of the United States, and the Associate Justices of the Supreme Court of the United States:

The petition for rehearing of Stimson Mill Company (hereinafter called Stimson) respectfully shows the following grounds not previously presented for allowance of the Writ of Certiorari:

I. Many taxpayers are being deprived of an opportunity to seek a conflicting decision in another Circuit

Court of Appeals, by reason of E.P.C. 16 which provides that relief may be denied without a detailed determination of normal earnings for separate years in cases where the Commissioner determines that his method of computing the constructive average would not result in a greater amount than the average under section 713 before reconstructing earnings under section 722.

II. It appears that respondent by recognizing or refusing to recognize the bar of section 732(c) to some extent seeks to control the jurisdiction of the courts.[1]

III. A procedural issue (as to whether the tax was paid before a claim for refund was filed) suggested in the Brief in Opposition, may have caused the Court to infer that if reviewed in this Court this case might be decided on that immaterial issue rather than on the issue presented in the petition, whereas such immaterial procedural issue is not properly before this Court.[1]

IV. The Committee Reports on the Revenue Bill of 1942 contain a specific explanation of the operation of section 722(b) (1) and show the method of granting relief in the case of a strike such as Stimson experienced, and it is submitted that the method of computation for which Stimson contends is in full accord with this explanation.

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[1] The Brief in Opposition was served on counsel for Stimson on Armistice Day, November 11, 1947, and the Court denied the Petition on November 17, 1947. In addition to constituting substantial grounds not previously presented as specified by Part 2 of the new Rule 33, as revised by this Court, points II and III, which in part arise by reason of the Brief in Opposition, might also be considered as being based on facts which are in the nature of circumstances of substantial effect intervening since the Petition herein was filed.

In the remainder of this petition for rehearing the above points are amplified.

I.

E.P.C. 16 issued by the Excess Profits Tax Council, which acts for the Commissioner in the administration of the relief provisions of section 722, provides in part as follows:

> "But a taxpayer which has established the existence of one or more of the factors set forth in section 722(b) (1), (2), (3), (4), or (5) *may be denied relief without a detailed and exact determination of normal earnings* when it is clear that without such a determination normal earnings would not exceed average base period net income." (Emphasis supplied).[2]

By assuming the power to include the computation of the constructive average as part of his discretionary determination of normal earnings, the Commissioner extends the statutory authority given him beyond the determination of normal earnings. His use of the expression "normal earnings" in the above quotation is with the meaning of "constructive average base period net income." When the Commissioner decides that the determination of normal earnings for separate years of the base period, averaged together as an ordinary arithmetic average, will probably result in an amount that is less

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[2] E.P.C. 16 is reported in the Internal Revenue Bulletin, C. B. 1947-1, p. 90. E.P.C. 16, dated June 2, 1947, was published in the Commerce Clearing House Reporter under date of June 11, 1947, the day after this case was argued in the Court of Appeals (R. p. 61) and was quoted, apparently with approval, by that Court in its opinion (R. p. 79, footnote 8).

than the average pursuant to the 75% rule of section 713 computed before correcting abnormalities under section 722, he now authorizes himself to refuse to compute normal earnings for separate years. It appears that the Commissioner is thus indicating that, in the case of another taxpayer deprived entirely of relief solely by the Commissioner's method of computing the constructive average, he never again will make the "mistake" of exercising his discretion to determine normal earnings for separate years as he did by stipulation in this case with respect to Stimson's earnings for 1937, and unless the Commissioner is forced by legal process to exercise his discretion and determine normal earnings for separate years in the case of another taxpayer, that is denied relief as in this case, it seems unlikely that the question as to the correct computation of the average for separate years could be brought before another Circuit Court of Appeals by such a taxpayer.

Furthermore, many taxpayers are represented before the Treasury Department only by a certified public accountant or an economist because of the technicalities involved in the determination of normal earnings for separate years. Even in the case at bar Stimson was represented by a certified public accountant in the Tax Court while the Commissioner was represented by four lawyers (Rec. p. 21). Such technical representatives of taxpayers cannot ordinarily be expected to be as thoroughly cognizant of the legal rights of their clients as lawyers, and may regard the denial of certiorari in this case as an authoritative approval by this Court of the Commissioner's computation of the constructive average. It seems probable that the cases of many taxpayers will be closed and

their rights foreclosed during the next two or three years before a taxpayer that is allowed relief on the basis of an ordinary arithmetic average may secure a conflicting decision in another Circuit Court of Appeals and a review by this Court.

The denial of relief to many taxpayers solely by reason of the Commissioner's computation of the average as in this case, seems particularly unjust in view of the fact that Congress in the statutory provisions here effective intended to remove limitations in the prior law so that relief might be given even in "cases involving relatively small tax savings."[3]

It is respectfully submitted that this case presents the issues involved in their simplest form. Since reconstructed earnings for 1937 have been stipulated there remains for determination here only the question of the proper computation of the constructive average. It is also respectfully submitted that an authoritative determination by this Court at an early date will preserve the rights of many taxpayers that are now threatened with a deprivation of their rights by E.P.C. 16.

II.

It is respectfully urged that point 2 of the Commissioner's argument in opposition presents the important question whether the Commissioner may to some extent

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[3] Quoted from Report of Finance Committee noted in footnote 5, C. B. 1942-2 p. 654, respecting amendment to Revenue Bill of 1942. The House receded with respect to this amendment, — Conference Report, H. R. Report No. 2586, Seventy-seventh Congress, Second Session, October 12, 1942, C. B. 1942-2 p. 701 at pp. 720, 721.

control the jurisdiction of the courts, by permitting review as in the *Pohatcong* case (infra), or by raising a bar to review as in this case whenever he chooses to seek the shelter of section 732(c) and hide his own lack of jurisdiction.

The question of the jurisdiction of this Court (which necessarily includes the jurisdiction of the Court of Appeals) is the first question presented by the Petition (Pet. p. 8). In stating that the Court of Appeals "was without jurisdiction under section 732(c)" (Br. in Opp. p. 6) the Commissioner is also denying the jurisdiction of the Supreme Court of the United States.

The Commissioner cites *Pohatcong Hosiery Mills, Inc.* v. *Commissioner*, C.C.A. 3, 1947, 162 F. (2d) 146 (Br. in Opp. p. 7), in which it appears that the Commissioner did not raise the question whether jurisdiction was barred by section 732(c) although the Court reviewed a procedural question involving subsection (d) of section 722. The Court said (at page 148):

> "As is immediately apparent, we are not here concerned with the merits of petitioner's claim for relief under section 722; we are concerned with the procedure for the realization of such relief."

It is submitted that the question whether section 732(c) precluded a review of a procedural question involving section 722(d) should at least have been presented and decided before the court in that case decided the procedural question. As shown in point III, infra, it also appears that the procedural issue suggested by the Brief in Opposition should properly be barred by section 732(c).

It is respectfully submitted that the extent to which

section 732(c) bars the jurisdiction of the courts should be authoritatively determined, and that the authoritative determination of the jurisdiction of the courts, as well as the authoritative determination of the limits of the Commissioner's discretionary jurisdiction, will not only aid the proper administration of the tax laws, but will also establish a needed precedent in the development of administrative law for the guidance of other administrative officers.

III.

It is respectfully submitted that the procedural issue suggested at pages 2 and 7 of the Brief in Opposition, as to whether the tax was paid before the claim for refund was filed, is not properly before this Court, and will not prevent a decision of this Court on the questions stated in the Petition (Pet. pp. 8-11) if the case is reviewed by this Court.

Procedural questions relating to the sufficiency of the application for relief as a claim for refund were not raised by the Commissioner in the Tax Court. His action on the merits of the claim for refund was a waiver of any irregularities therein (*Tucker* v. *Alexander,* 1927, 275 U.S. 228, 231, 72 L. ed. 253, 256) including any payment made after filing the claim for refund (*Continental Illinois National Bank* v. *United States,* Court of Claims 1941, 39 F. Supp. 620, 623) and was presumptive proof of all acts necessary to make that action legally operative (*R. H. Stearns Co.* v. *United States* 1934, 291 U.S. 54, 63; 78 L. ed. 647, 653). Stimson's claim for refund was not rejected because it was filed before the tax was paid as was the

case in *Pohatcong Hosiery Mills, Inc.* v. *Commissioner*, C.C.A. 3, 1947, 162 F. (2d) 146, 147. The Commissioner sent Stimson a notice of disallowance of the claim (Rec. p. 7) and thus determined that the claim had met the requirements of section 722(d). In the Tax Court the Commissioner failed to raise any objection and did not deny that his determination was correct.

The Commissioner stipulated that the tax was overpaid if the average is computed as petitioner claims it should be, and the Tax Court adopted the stipulation as a finding of fact (Rec. p. 27). It was a finding that the petitioner would recover something—that the claim met the requirements of section 722(d). It is submitted that such determination was a determination of a question of fact necessary solely by reason of section 722, of which section 722(d) is a part, and that *review of such a fact determination under section 722 by the Courts (other than the Tax Court) is precluded by section 732(c)*. It was not a question of whether the Commissioner had exceeded the statutory bounds of his discretionary jurisdiction, as Stimson submits is the question herein relating to the computation of the constructive average.

The record shows that the amount of the deficiency, $2,106.08, was paid after the application for relief was filed. *Some tax had been paid before the application was filed,* and that was a sufficient basis for relief (*Uni-Term Stevedoring Co.* v. *Commissioner,* 3 T.C. 917, 919). From the record the amount of overpayment can be computed as $5,759.70 subject to adjustment for the 10% post-war credit (Pet. pp. 5, 6); and from any standpoint an overpayment of excess profits tax results even if the amount of the deficiency be excluded from the computation.

In accordance with the stipulation (Rec. p. 27) as well as in accordance with the rules of the Tax Court, it appears that the amount of a refund would be computed after a remand of the case to the Tax Court if this Court should find the issue as to the proper computation of the average in Stimson's favor. It is submitted that if a writ of certiorari should be granted herein the procedural issue suggested by the Commissioner would not prevent a decision of this Court on the jurisdiction issue or the issue as to the computation of the average.

IV.

At pages 8 and 9 of the Brief in Opposition it is said that "There is nothing in the legislative history which justifies" the conclusion argued by Stimson that the constructive average is required to be computed in the manner provided by section 713. It is respectfully submitted that the report of the Committee on Ways and Means contains the following specific explanation of the operation of section 722(b) (1) in the case of a strike such as Stimson experienced:[4]

> "If in one or more taxable years in the base period the normal production, or output, or operation was interrupted or diminished because there occurred immediately prior to or during the base period events unusual and peculiar to the experience of the taxpayer, it may obtain this relief. An example of such an occurrence would be a fire, a flood, or a strike. If as a re-

[4] Committee on Ways and Means Report No. 2333, Seventy-seventh Congress, First Session, accompanying the Revenue Bill of 1942, as reported in Internal Revenue Bulletin — Cumulative Bulletin, 1942-2, p. 391.

sult of a fire in 1938 the earnings in 1939 were abnormally low, *there might be substituted for 1939* an amount approximating what the volume of business would have been if the fire had not occurred. This relief is similar to the relief granted under section 722 of the present law." (Emphasis supplied).

Also with regard to the operation of the statute in the same situation the report of the Committee on Finance[3] stated:

> "This is an expression of the same situation for which relief is granted under existing law, . . ."

The "present law" and the "existing law" are the 1941 enactment of section 722 which admittedly required the constructive average to be computed in the manner prescribed by section 713. Before relief is granted under the 1942 enactment the average must be computed under section 713. The only difference between that average and the constructive average indicated by the above quotation is the *substitution* there stated. Normal earnings established for one year of the base period are "substituted" for the excess profits net income for that year (as explained at the top of page 19 of the argument in support of the petition).

A "hybrid credit" results when relief is granted under section 722, either pursuant to the Commissioner's method of computing the constructive average and then taking 95% thereof under section 713, or pursuant to the statu-

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[3] Senate Report No. 1631, Seventy-seventh Congress, Second Session, accompanying the Revenue Bill of 1942 as reported in Internal Revenue Bulletin — Cumulative Bulletin, 1942-2, pp. 649-650.

tory method for which Stimson contends. The issue here, which involves questions as to the limits of jurisdiction and discretion, is which hybrid credit is proper.

Wherefore petitioner prays this Court to reconsider its petition and, if this Court now deems it proper so to do, to vacate the judgment denying such petition and to issue a Writ of Certiorari to review the judgment of the United States Circuit Court of Appeals for the Ninth Circuit in the instant case entered July 21, 1947.

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APPENDIX.

Sections 722(d) and 732(c)
of the
Internal Revenue Code as Amended

Sec. 722(d)[6] *Application for Relief Under This Section.* The taxpayer shall compute its tax, file its return, and pay the tax shown on its return under this subchapter without the application of this section, except as provided in section 710(a) (5). The benefits of this section shall not be allowed unless the taxpayer within the period of time prescribed by section 322 and subject to the limitation as to amount of credit or refund prescribed in such section makes application therefor in accordance with regulations prescribed by the Commissioner with the approval of the Secretary. If a constructive average base period net income has been determined under the provisions of this section for any taxable year, the Commissioner may, by regulations approved by the Secretary, prescribe the extent to which the limitations prescribed by this subsection may be waived for the purpose of determining the tax under this subchapter for a subsequent taxable year.

* * * * *

Sec. 732(c) (26 U.S.C.A. Sec. 732(c)) *Finality of determination.* If in the determination of the tax liability under this subchapter the determination of any question is necessary solely by reason of section 711(b) (1) (H), (I), (J), or (K), section 721, or section 722, the determination of such question shall not be reviewed or redetermined by any court or agency except the Board.

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[6] Sec. 722(d) was amended to its present language by Act of December 17, 1943, C. 346, 57 Stat. 601 — 26 U.S.C.A. Internal Revenue Acts beginning 1940 p. 417. That Act makes this amendment applicable with respect to taxable years beginning after December 31, 1939.